

ORIGINAL



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BEFORE THE ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
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IN THE MATTER OF THE APPLICATION OF
SAHUARITA WATER COMPANY, LLC, FOR
A DETERMINATION OF THE CURRENT
FAIR VALUE OF ITS UTILITY PROPERTY
AND FOR THE ESTABLISHMENT OF JUST
AND REASONABLE RATES AND
CHARGES.

DOCKET NO. W-03718A-15-0213

**STAFF'S NOTICE OF FILING
SURREBUTTAL TESTIMONY**

Staff of the Arizona Corporation Commission ("Staff") hereby files the Surrebuttal Testimony
of Staff Witnesses Teresa B. Hunsaker, Michael S. Thompson and Crystal S. Brown in the above
docket.

RESPECTFULLY SUBMITTED this 1st day of April 2016.

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Original and thirteen (13) copies
of the foregoing filed this
1st day of April 2016 with:

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Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Copy of the foregoing emailed/mailed
this 1st day of April 2016 to:

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Arizona Corporation Commission
DOCKETED

APR 01 2016

DOCKETED BY

BEFORE THE ARIZONA CORPORATION COMMISSION

DOUG LITTLE

Chairman

BOB STUMP

Commissioner

BOB BURNS

Commissioner

TOM FORESE

Commissioner

ANDY TOBIN

Commissioner

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SAHUARITA WATER COMPANY, LLC, FOR A)
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REASONABLE RATES AND CHARGES.)

DOCKET NO. W-03718A-15-0213

SURREBUTTAL

TESTIMONY

OF

TERESA B. HUNSAKER

PUBLIC UTILITIES ANALYST

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

APRIL 1, 2016

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EXECUTIVE SUMMARY
SAHUARITA WATER COMPANY, LLC
DOCKET NO. W-03718A-15-0213

Staff's surrebuttal testimony recommends rates that would increase operating revenues by \$166,419 to produce operating revenues of \$3,063,165 resulting in operating income of \$122,456 or a 5.75 percent increase over test year revenues of \$2,896,746. Staff also recommends a revised original cost rate base ("OCRB") of \$9,359,714. Staff's recommend rate of return is 8.41 percent.

Staff's direct testimony recommended rates that would increase operating revenues by \$70,562 to produce operating revenues of \$2,967,308.

Typical Bill Analysis

The typical 5/8 x 3/4-inch meter residential customers with a median usage of 4,500 gallons would experience a \$2.18 or a 7.18 percent increase in their monthly bill, from \$30.28 to \$32.45, under Staff's surrebuttal recommended rates.

1 **I. INTRODUCTION**

2 **Q. Please state your name, occupation, and business address.**

3 A. My name is Teresa B. Hunsaker. I am a Public Utilities Analyst III employed by the Arizona
4 Corporation Commission ("ACC" or "Commission") in the Utilities Division ("Staff"). My
5 business address is 1200 West Washington Street, Phoenix, Arizona 85007.

6
7 **Q. Are you the same Teresa B. Hunsaker who filed direct testimony in this case?**

8 A. Yes, I am.
9

10 **II. PURPOSE OF SURREBUTTAL TESTIMONY**

11 **Q. What is the purpose of your surrebuttal testimony in this proceeding?**

12 A. The purpose of my surrebuttal testimony in this proceeding is to respond, on behalf of Staff,
13 to the rebuttal testimony of Sahuarita Water Company ("SWC" or "Company") witnesses Mr.
14 Geoff Caron and Mr. Thomas J. Bourassa regarding revenue requirement, rate base, and
15 operating revenues and expenses.

16
17 **Q. Did you attempt to address every issue raised by the Company in its rebuttal
18 testimony?**

19 A. No. I limited my discussion to certain issues as outlined below. My silence on any particular
20 issue raised in the Company's rebuttal testimony does not indicate that I agree with the
21 Company's stated rebuttal position on the issue. Rather, where I do not respond, I rely on
22 my direct testimony.
23

III. SUMMARY OF PROPOSED REVENUES

Q. Has Staff reviewed Mr. Bourassa's rebuttal testimony regarding revenue requirement for the Company?

A. Yes.

Q. Please summarize the proposed and recommended revenue requirement, revenue increases, and percentage increase.

A. The proposed and recommended revenue requirement, revenue increase, and percentage increase are as follows:

	<u>Revenue Requirement</u>	<u>Revenue Increase</u>	<u>% Increase</u>
Company - Direct	\$3,229,480	\$332,733	11.49%
Staff - Direct	\$2,967,308	\$70,562	2.44%
Company - Rebuttal	\$3,173,385	\$276,638	9.55%
Staff - Surrebuttal	\$3,063,165	\$166,419	5.75%

Q. What are the primary reasons why the Company's revenue requirement is higher and proposed increase larger than Staff's recommendation?

A. The difference in revenue requirement is primarily a result of the differences in plant in service, cost of capital, and operating expenses.

IV. RATE BASE

Q. Has Staff reviewed Mr. Bourassa's rebuttal testimony regarding rate base for the Company?

A. Yes. The Company's filing treats the original cost rate base ("OCRB") the same as the fair value rate base ("FVRB").

1 **Q. Would Staff please identify the respective rate base proposed by the Company and**
2 **recommended by Staff?**

3 A. Yes, the rate bases proposed by the Company and recommended by Staff are as follows:
4

	<u>OCRB/FVRB</u>
Company - Direct	\$9,298,032
Staff - Direct	\$8,778,456
Company - Rebuttal	\$9,359,714
Staff - Surrebuttal	\$9,359,714

5
6 **Q. What changes did Staff make to Rate Base in surrebuttal testimony?**

7 A. Staff made changes to the following adjustments:
8

- 9 1. Rate Base Adjustment No. 1 – Plant Reclassifications
- 10 2. Rate Base Adjustment No. 2 – Plant Additions and Retirements
- 11 3. Rate Base Adjustment No. 4 - Accumulated Depreciation (“A/D”)
- 12 4. Rate Base Adjustment No. 5a – Contributions in Aid of Construction (“CIAC”) and
13 Accumulated Amortization
- 14 5. Rate Base Adjustment No. 5b – Accumulated Deferred Income Taxes (“ADIT”)
15

16 **Q. Will Staff please discuss the Company’s proposed OCRB?**

17 A. Yes. Staff worked directly with the Company after Staff’s direct testimony was filed to
18 correct the Company’s proposed OCRB. The Company has detailed these changes in its
19 rebuttal testimony by both of the Company’s witnesses. Based on these discussions and
20 responses by the Company to Staff’s data requests, Staff and the Company were able to
21 resolve the issues in the OCRB. Staff will address the rebuttal rate base adjustments to
22 OCRB to Plant in Service (“PIS”), Accumulated Depreciation (“A/D”), Contribution in Aid

1 of Construction ("CIAC") and Accumulated Amortization, and Accumulated Deferred
2 Income Taxes ("ADIT").
3

4 *Plant in Service ("PIS")*

5 **Q. Does Staff concur with the Company's proposed PIS adjustments in the Company's**
6 **rebuttal testimony?**

7 A. Yes. Staff worked directly with the Company to properly reflect the following as shown in
8 Staff's Adjustments No. 1 and No. 2:
9

- 10 1. Reverse the retirements for arsenic media;
- 11 2. Reclassification of the arsenic media costs and water treatment equipment;
- 12 3. Reclassification of the original arsenic media costs; and,
- 13 4. Retirement of original arsenic media.
14

15 **Q. Does Staff concur with the Company's proposed rebuttal treatment of the**
16 **reclassification of the original arsenic media costs to a separate plant account?**

17 A. Yes. Staff concurs with the Company that the useful life for the original arsenic media costs
18 is approximately 15 years.
19

20 **Q. Does Staff concur with the Company's reclassification of the Water Treatment**
21 **Equipment?**

22 A. Yes. Staff concurs with the Company's reversal of the \$120,000 retirement of arsenic media
23 costs as shown in Staff's Adjustment No. 2.
24

Accumulated Depreciation ("A/D")

Q. Does Staff concur with the Company's proposed A/D adjustments in the Company's rebuttal testimony?

A. Yes. Staff concurs with the Company's proposed A/D adjustments. Due to the proposed adjustments to PIS, the proposed A/D adjustments are appropriate as reflected in the plant reconstruction provided by the Company as shown in Staff's Adjustment No. 4.

Contributions in Aid of Construction ("CIAC")

Q. Does Staff concur with the Company's proposed adjustments to CIAC and/or Accumulated Amortization?

A. Yes. Staff concurs with the Company's proposed CIAC adjustments to the accumulated amortization as shown in Staff's Adjustment No. 5a.

Accumulated Deferred Income Taxes ("ADIT")

Q. Does Staff concur with the Company's proposed adjustments to ADIT?

A. Yes. Staff concurs with the Company's proposed adjustments to ADIT in Staff's Adjustment No. 5b.

V. OPERATING INCOME

Q. What changes did Staff make to Operating Income in its surrebuttal testimony?

A. Staff made changes to the following adjustments:

1. Operating Income Adjustment No. 7 – Depreciation Expense
2. Operating Income Adjustment No. 9 – Income Tax Expense

1 **Q. Has Staff reviewed Mr. Bourassa's rebuttal testimony regarding revenue and expenses**
2 **for the Company?**

3 A. Yes.

4
5 **Q. Does Staff concur with all of the Company's expense adjustments in the Company's**
6 **rebuttal testimony?**

7 A. No. Staff's depreciation expense is only different due to rounding, and Staff will address the
8 Company's rebuttal testimony regarding incentive pay bonuses to contract employees.

9
10 *Depreciation Expense*

11 **Q. Please describe the total difference in Staff's depreciation expense to the Company's**
12 **depreciation expense.**

13 A. Staff depreciated Original Arsenic Media – Plant Account 320.4 at 6.67 percent as shown on
14 Schedule TBH-18. Staff's total adjusted depreciation expense for the test year is \$22,028.
15 The Company depreciated Original Arsenic Media – Plant Account 320.4 at 6.66 percent on
16 Rebuttal Schedule C-2, Page 2. The Company's total adjusted depreciation expense for the
17 test year is \$22,049. The total difference is \$21.

18
19 *Contractual Services – Management Fees Expense*

20 **Q. Does Staff concur with the Company's proposed contractual services – management**
21 **fees expense adjustment for bonuses in the Company's rebuttal testimony?**

22 A. No. Staff continues to disagree with the inclusion of incentive pay bonuses with payroll taxes
23 for non-dedicated and dedicated employees of Rancho Sahuarita Management Company
24 ("RSMC"). Staff removed all incentive pay bonuses for both non-dedicated and dedicated
25 contract employees in the amount of \$21,470. RSMC has steadily increased the salaries of the
26 contract employees over the years as their duties and responsibilities have changed. Through

1 numerous data requests provided by the Company, Staff reviewed the salary increases without
2 bonuses over several years (Projected 2015, Test Year 2014 and 2013) and the increases
3 varied from approximately 0.5 percent to approximately 18.0 percent. The national average
4 in 2015 for pay increases has projected an increase of 3.0 percent.

5
6 **Q. Did Staff review the distribution of the incentive pay bonuses to dedicated employees**
7 **in 2014? Please explain.**

8 A. Yes. Staff reviewed the distribution of incentive pay bonuses to non-dedicated and dedicated
9 contract employees covered by RSMC. Approximately 66 percent of these bonuses were paid
10 to seven dedicated contract employees (13 total employees) including one employee that is
11 allocated at 89 percent to the Company directly. The dedicated employees in managerial or
12 supervisory roles consisted of four employees that were provided with approximately 95
13 percent of these bonuses.

14
15 **Q. Did Staff review the distribution of the incentive pay bonuses to non-dedicated**
16 **employees in 2014? Please explain.**

17 A. Yes. The four non-dedicated employees received approximately 38 percent of their entire
18 bonuses from the Company and 62 percent from an affiliate Company. However, the
19 Company has been allocated from 10 percent to 30 percent of their salary and benefits.

20
21 **Q. Has Staff been provided with incentive plans or documentation to support that**
22 **bonuses are part of the total compensation package?**

23 A. No. In the Company's response to Data Request TBH 1.34b, the Company stated that
24 "There is nothing in writing and it is entirely up to the Managing Partner. Items that are
25 considered are overall performance and vehicle use. During the year, employees are not

1 reimbursed for the use of their private vehicles and this is also taken into consideration at the
2 end of the year.” Staff has provided a copy of this data request in Attachment A.
3

4 **Q. What is Staff’s recommendation?**

5 A. Staff continues to recommend that no incentive pay bonuses to dedicated or non-dedicated
6 contract employees be funded by rate payers. Staff recommends that all contract employees
7 be required to properly account for the use of their personal vehicles for business purposes
8 and be reimbursed by the Company.
9

10 *Income Taxes Expense*

11 **Q. Did Staff make any corrections in its schedule to test year Income Tax Expense?**

12 A. Yes. Staff inadvertently linked the wrong tax rates in direct testimony that created an error in
13 Adjustment No. 9. Staff has properly linked the appropriate tax rates in surrebuttal testimony
14 and schedules.
15

16 **Q. Did Staff make an adjustment to test year Income Tax Expense?**

17 A. Yes. Staff applied the Company’s income tax rates as provided on the Company’s Schedule
18 C-3, Page 2 for this LLC to Staff’s adjusted test year taxable income. Income tax expenses
19 for the test year and recommended revenues are shown on Schedules TBH-11 and TBH-20.
20

21 **VI. RATE DESIGN**

22 **Q. What is Staff’s recommended rate design for water service?**

23 A. The Staff’s recommended rates are shown on Surrebuttal Schedule TBH-21, pages 1 and 2.
24

1 **Q. Did Staff review the recommended revenue requirement generated in direct testimony**
2 **as discussed by the Company in its rebuttal testimony?**

3 A. Yes. Staff reviewed the recommended revenue requirement through Staff's recommended
4 rate design. Due to Staff's acceptance of the Company's usage normalization and revenue
5 annualization, Staff adjusted the rate design in surrebuttal to take into consideration these
6 adjustments to revenue.

7
8 **Q. What is the rate impact on a typical 5/8 x 3/4-inch meter residential customer with**
9 **median usage in Staff's recommended surrebuttal rates?**

10 A. The typical 5/8 x 3/4-inch meter residential customers with a median usage of 4,500 gallons
11 would experience a \$2.18 or a 7.18 percent increase in their monthly bill, from \$30.28 to
12 \$32.45, under Staff's recommended rates. A typical bill analysis is provided on Schedule
13 TBH-22.

14
15 **Q. Does this conclude your surrebuttal testimony?**

16 A. Yes, it does.

SAHUARITA WATER COMPANY LLC

Docket No. W-03718A-15-0213

Test Year December 31, 2014

SURREBUTTAL TESTIMONY OF TERESA B. HUNSAKER

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TBH-19	OPERATING INCOME ADJUSTMENT No. 8 - Property Taxes Expense
TBH-20	OPERATING INCOME ADJUSTMENT NO. 9 - Income Tax Expense

SAHUARITA WATER COMPANY LLC
Docket No. W-03718A-15-0213
Test Year December 31, 2014

Surrebuttal Schedule TBH-1

REVENUE REQUIREMENT

LINE NO.	DESCRIPTION	[A]	[B]
		COMPANY ORIGINAL COST	STAFF ORIGINAL COST
1	Adjusted Rate Base	\$9,298,032	\$9,359,714
2	Adjusted Operating Income (Loss)	\$598,003	\$664,683
3	Current Rate of Return (L2 / L1)	6.43%	7.10%
4	Required Rate of Return	9.20%	8.41%
5	Required Operating Income (L4 * L1)	\$855,419	\$787,140
6	Operating Income Deficiency (L5 - L2)	\$257,416	\$122,456
7	Gross Revenue Conversion Factor	1.2926	1.3590
8	Required Revenue Increase (L7 * L6)	\$332,734	\$166,419
9	Adjusted Test Year Revenue	\$2,896,746	\$2,896,746
10	Proposed Annual Revenue (L8 + L9)	\$3,229,480	\$3,063,165
11	Required Increase in Revenue (%)	11.49%	5.75%

References:

Column [A]: Company Schedule B-1

Column [B]: Staff Schedules OCRB, GRCE, TYOI & COC

GROSS REVENUE CONVERSION FACTOR

Line No.	Description	[A]	[B]	[C]	[D]	[E]	[F]
<i>Calculation of Gross Revenue Conversion Factor:</i>							
1	Revenue	100.0000%					
2	Uncollectible Factor (Line 11)	0.0000%					
3	Revenues (L1 - L2)	100.0000%					
4	Combined Federal and State Income Tax and Property Tax Rate (L23)	26.4168%					
5	Subtotal (L3 - L4)	73.5832%					
6	Revenue Conversion Factor (L1 / L5)	1.359005					
<i>Calculation of Uncollectible Factor:</i>							
7	Unity	100.0000%					
8	Combined Federal and State Tax Rate (L17)	25.0817%					
9	One Minus Combined Income Tax Rate (L7 - L8)	74.9183%					
10	Uncollectible Rate	0.0000%					
11	Uncollectible Factor (L9 * L10)		0.0000%				
<i>Calculation of Effective Tax Rate:</i>							
12	Operating Income Before Taxes (Arizona Taxable Income)	100.0000%					
13	Arizona State Income Tax Rate (L57 Col E)	3.3693%					
14	Federal Taxable Income (L12 - L13)	96.6307%					
15	Applicable Federal Income Tax Rate (L56 Col E)	22.4694%					
16	Effective Federal Income Tax Rate (L14 * L15)	21.7123%					
17	Combined Federal and State Income Tax Rate (L13 + L16)		25.0817%				
<i>Calculation of Effective Property Tax Factor:</i>							
18	Unity	100.0000%					
19	Combined Federal and State Income Tax Rate (L17)	25.0817%					
20	One Minus Combined Income Tax Rate (L18 - L19)	74.9183%					
21	Property Tax Factor	1.7821%					
22	Effective Property Tax Factor (L20 * L21)		1.3351%				
23	Combined Federal and State Income Tax and Property Tax Rate (L17 + L22)			26.4168%			
24	Required Operating Income (Schedule TBH-1, L5)	\$ 787,140					
25	Adjusted Test Year Operating Income (Loss) (Schedule TBH-10, L32)	\$ 664,683					
26	Required Increase in Operating Income (L24 - L25)		\$ 122,456				
27	Income Taxes on Recommended Revenue (Col. [F], L52)	\$ 156,892					
28	Income Taxes on Test Year Revenue (Col. [C], L52)	\$ 115,895					
29	Required Increase in Revenue to Provide for Income Taxes (L27 - L28)		\$ 40,997				
30	Recommended Revenue Requirement (Schedule TBH-1, L10)	\$ 3,063,165					
31	Uncollectible Rate (L10)	0.0000%					
32	Uncollectible Expense on Recommended Revenue (L24 * L25)	\$ 0					
33	Adjusted Test Year Uncollectible Expense	\$ 0					
34	Required Increase in Revenue to Provide for Uncollectible Exp.		\$ 0				
35	Property Tax with Recommended Revenue (Schedule TBH-19, L19)	\$ 157,528					
36	Property Tax on Test Year Revenue (Schedule TBH-19, L20)	\$ 154,562					
37	Increase in Property Tax Due to Increase in Revenue (L35 - L36) (Schedule TBH-19, L21)		\$ 2,966				
38	Total Required Increase in Revenue (L26 + L29 + L34 + L37)	\$ 166,419					

	(A)	(B)	(C)	(D)	(E)	(F)
		Test Year		Staff Recommended		
		Total	Water	Total		Water
39	Revenue	\$2,896,746	\$2,896,746	\$3,063,165		\$3,063,165
40	Operating Expenses Excluding Income Taxes	2,116,169	2,116,169	2,119,134		2,119,134
41	Synchronized Interest (L47)	80,494	80,494	80,494		80,494
42	Arizona Taxable Income (L39 - L40 - L41)	\$ 700,084	\$ 700,084	\$ 863,537		\$ 863,537
43	Arizona State Effective Income Tax Rate (see Company Schedule C-3, Page 2)	2.7401%	2.7401%	2.8592%		2.8592%
44	Arizona Income Tax (L42 * L43)	\$ 19,183	\$ 19,183	\$ 24,690		\$ 24,690
45	Federal Taxable Income (L42 - L44)	\$ 680,901	\$ 680,901	\$ 838,846		\$ 838,846
46	Federal Tax Rate (see Company Schedule C-3, Page 2)	14.2034%	14.2034%	15.7598%		15.7598%
47	Federal Tax	\$ 96,711	\$ 96,711	\$ 132,201		\$ 132,201
48						
49						
50						
51						
52						
53	Total Federal Income Tax	\$ 96,711	\$ 96,711	\$ 132,201		\$ 132,201
54	Combined Federal and State Income Tax (L35 + L42)	\$ 115,895	\$ 115,895	\$ 156,892		\$ 156,892
55	COMBINED Applicable Federal Income Tax Rate [Col. [D], L53 - Col. [A], L53] / [Col. [D], L45 - Col. [A], L45]			22.4694%		
56	Applicable Federal Income Tax Rate [Col. [F], L53 - Col. [C], L53] / [Col. [F], L45 - Col. [C], L45]				22.4694%	
57	Applicable State Income Tax Rate [Col. [F], L44 - Col. [C], L44] / [Col. [F], L42 - Col. [C], L42]				3.3693%	

Calculation of Interest Synchronization:

58	Rate Base	
59	Weighted Average Cost of Debt	
60	Synchronized Interest (L59 * L60)	

Wastewater	Water
\$0	\$9,359,714
0.0000%	0.8600%
\$0	\$80,494

RATE BASE - ORIGINAL COST/FAIR VALUE

LINE NO.	DESCRIPTION	[A]	[B]	REF	[C]
		COMPANY AS FILED	STAFF ADJUSTMENTS		STAFF AS ADJUSTED
1	Plant in Service	\$27,468,728	(\$39,152)	1,2,3	\$27,429,576
2	Less: Accumulated Depreciation	6,309,380	(161,732)	4	6,147,648
3	Net Plant in Service	<u>\$21,159,348</u>	<u>122,579</u>		<u>\$21,281,927</u>
<u>LESS:</u>					
4	Net Contribution in Aid-of Construction (CIAC)	\$6,335,865	\$22,097	5a	\$6,357,962
5	Advances in Aid of Construction (ALAC)	5,189,497	0		5,189,497
6	Customer Deposits	52,876	0		52,876
7	Accumulated Deferred Income Taxes (ADIT)	283,077	38,801	5b	321,878
	Total Deductions	<u>\$11,861,315</u>	<u>\$60,898</u>		<u>\$11,922,213</u>
<u>ADD:</u>					
8	Unamortized Finance Charges	\$0	\$0		\$0
9	Deferred Tax Assets	0	0		0
10	Allowance for Working Capital	0	0		0
11	Rounding	(1)	1		0
	Total Additions	<u>(\$1)</u>	<u>\$1</u>		<u>\$0</u>
12	Original Cost Rate Base	<u>\$9,298,032</u>	<u>61,682</u>		<u>\$9,359,714</u>

References:

Column [A]: Company Schedule B-1

Column [B]: Schedule TBH-4

Column [C]: Column [A] + Column [B]

SUMMARY OF ORIGINAL COST RATE BASE ADJUSTMENTS

LINE NO.	ACCT. NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] Plant Reclass ADJ No. 1	[C] Plant Add and Retire ADJ No. 2	[D] Post-Test Year ADJ No. 3	[E] Accum. Dep. ADJ No. 4	[F] CIAC ADJ No. 5a	[G] ADIT ADJ No. 5b	[H] STAFF ADJUSTED
				Ref. Sch TBH-5	Ref. Sch TBH-6	Ref. Sch TBH-7	Ref. Sch TBH-8	Ref. Sch TBH-9a	Ref. Sch TBH-9b	
PLANT IN SERVICE:										
1	301	Organization Costs	\$7,541	\$0	\$0	\$0	\$0	\$0	\$0	\$7,541
2	302	Franchise Costs	352,403	0	0	0	0	0	0	352,403
3	303	Land & Land Rights	13,636	0	0	0	0	0	0	13,636
4	304	Structures & Improvements	401,832	0	0	0	0	0	0	401,832
5	307	Wells & Springs	2,142,644	0	0	0	0	0	0	2,142,644
6	310	Power Generation Equipment	549,708	0	0	0	0	0	0	549,708
7	311	Electric Pumping Equipment	195,407	0	0	0	0	0	0	195,407
8	320	Water Treatment Equipment	2,001,053	(2,121,053)	120,000	0	0	0	0	0
9	320.1	Water Treatment Plants	0	1,499,569	0	0	0	0	0	1,499,569
10	320.2	Solutions & Feeders	0	46,479	0	0	0	0	0	46,479
11	320.3	Arsenic Media	152,307	(152,307)	0	0	0	0	0	0
12	320.4	Original Arsenic Media	0	575,005	(157,503)	0	0	0	0	417,503
13	320.5	Regenerated Arsenic Media	0	152,307	0	(1,650)	0	0	0	150,657
14	330	Distribution Reservoirs & Standpipes	1,848,872	(1,848,872)	0	0	0	0	0	0
15	330.1	Storage Tank	0	1,811,998	0	0	0	0	0	1,811,998
16	330.2	Pressure Tanks	0	36,874	0	0	0	0	0	36,874
17	331	Transmission & Distribution Mains	13,281,053	0	0	0	0	0	0	13,281,053
18	333	Services	2,256,719	0	0	0	0	0	0	2,256,719
19	334	Meters & Meter Installations	1,489,172	0	0	0	0	0	0	1,489,172
20	335	Hydrants	732,251	0	0	0	0	0	0	732,251
21	336	Backflow Prevention Devices	1,660	0	0	0	0	0	0	1,660
22	339	Other Plant & Misc. Equip.	0	0	0	0	0	0	0	0
23	340	Office Furniture & Fixtures	160,855	0	0	0	0	0	0	160,855
24	340.1	Computer & Software	122,607	0	0	0	0	0	0	122,607
25	341	Transportation Equipment	139,706	0	0	0	0	0	0	139,706
26	342	Store Equipment	0	0	0	0	0	0	0	0
27	343	Tools & Work Equipment	37,840	0	0	0	0	0	0	37,840
28	344	Laboratory Equipment	132	0	0	0	0	0	0	132
29	345	Power Operated Equipment	0	0	0	0	0	0	0	0
30	345	Communications Equipment	577,721	0	0	0	0	0	0	577,721
31	347	Miscellaneous Equipment	695	0	0	0	0	0	0	695
32	348	Other Intangibles	1,002,914	0	0	0	0	0	0	1,002,914
33	Gross Utility Plant in Service		\$27,468,728	\$0	(\$37,503)	(\$1,650)	\$0	\$0	\$0	\$27,429,576
34	Less: Accumulated Depreciation		6,309,380	0	0	0	(161,732)	0	0	6,147,648
35	Net Utility Plant in Service (L29 - L30)		\$21,159,348	\$0	(\$37,503)	(\$1,650)	\$161,732	\$0	\$0	\$21,281,927
DEDUCTIONS:										
36	Contributions in Aid of Construction (CIAC)		\$7,712,717	\$0	\$0	\$0	\$0	\$0	\$0	\$7,712,717
37	Less: Accumulated Amortization		1,376,852	0	0	0	0	(22,097)	0	1,354,755
38	Net CIAC (L32 - L33)		\$6,335,865	\$0	\$0	\$0	\$0	\$22,097	\$0	\$6,357,962
39	Advances in Aid of Construction (AIAC)		5,189,497	0	0	0	0	0	0	5,189,497
40	Customer Meter Deposits		52,876	0	0	0	0	0	0	52,876
41	Accumulated Deferred Income Taxes (ADIT)		283,077	0	0	0	0	0	38,801	321,878
42	Total Deductions		\$11,861,315	\$0	\$0	\$0	\$0	\$22,097	\$38,801	\$11,922,213
ADDITIONS:										
43	Unamortized Finance Charges		\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
44	Deferred Tax Assets		0	0	0	0	0	0	0	0
45	Allowance for Working Capital		0	0	0	0	0	0	0	0
46	Rounding		(1)	0	0	0	0	0	1	0
47	Total Additions		(\$1)	\$0	\$0	\$0	\$0	\$0	\$1	\$0
48	ORIGINAL COST RATE BASE		\$9,298,032	\$0	(\$37,503)	(\$1,650)	\$161,732	(\$22,097)	(\$38,800)	\$9,359,714

ADJ No.	Schedule
1	TBH-5
2	TBH-6
3	TBH-7
4	TBH-8
5a	TBH-9a
5b	TBH-9b

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Surrebuttal Schedule TBH-5

RATE BASE ADJUSTMENT NO. 1 - Plant Reclassification				
LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] ADJUSTMENT	[C] STAFF ADJUSTED
1	Water Treatment Equipment	\$2,001,053	(2,121,053)	(\$120,000)
2	Water Treatment Plants	0	1,499,569	1,499,569
3	Solutions & Feeders	0	46,479	46,479
4	Arsenic Media	152,307	(152,307)	0
5	Original Arsenic Media	0	575,005	575,005
6	Regenerated Arsenic Media	0	152,307	152,307
7	Distribution Reservoirs & Standpipes	1,848,872	(1,848,872)	0
8	Storage Tank	0	1,811,998	1,811,998
9	Pressure Tanks	0	36,874	36,874

REFERENCES:

Column [A]: Company Schedule B-2

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-6

RATE BASE ADJUSTMENT NO. 2 - Plant Additions and Retirements

LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] ADJUSTMENT	[C] STAFF ADJUSTED
1	Original Arsenic Media Additions (Batch 3.0)	\$0	\$130,000	\$130,000
2	Original Arsenic Media Retirement (original - Batch 1.0)	0	(287,503)	(287,503)
3	Water Treatment Equipment (Misclassified)	0	120,000	120,000
4	Total	\$0	(\$37,503)	(\$37,503)

REFERENCES:

Column [A]: Company Schedule B-2

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-7

RATE BASE ADJUSTMENT NO. 3 - Post-Test Year Plant				
LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] ADJUSTMENT	[C] STAFF ADJUSTED
1	Regenerated Arsenic Media	\$152,307	(\$1,650)	\$150,657

REFERENCES:

Column [A]: Company Schedule B-2
Column [B]: Testimony TBH
Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-8

RATE BASE ADJUSTMENT NO. 4 - Accumulated Depreciation				
LINE		[A]	[B]	[C]
NO.	DESCRIPTION	COMPANY AS FILED	ADJUSTMENT	STAFF ADJUSTED
1	Accumulated Depreciation	\$6,309,380	(\$161,732)	\$6,147,648

REFERENCES:

Column [A]: Company Schedule B-2

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-9a

RATE BASE ADJUSTMENT NO. 5a - Contributions in Aid of Construction ("CIAC") Amortization				
LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENT	[C] STAFF RECOMMENDED
1	CIAC Amortization	\$1,376,852	(\$22,097)	\$1,354,755
2	Total	\$1,376,852	(\$22,097)	\$1,354,755

References:

Column [A]: Company Schedule C-2 & Workpapers

Column [B]: Testimony TBH, Company Rebuttal Schedule B-2

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-9b

RATE BASE ADJUSTMENT NO. 5b - Accumulated Deferred Income Taxes ("ADIT")				
LINE		[A]	[B]	[C]
NO.	DESCRIPTION	COMPANY	STAFF	STAFF
		PROPOSED	ADJUSTMENT	RECOMMENDED
1	ADIT	\$283,077	\$38,801	\$321,878
2	Total	\$283,077	\$38,801	\$321,878

References:

Column [A]: Company Schedule C-2 & Workpapers

Column [B]: Testimony TBH, Company Rebuttal Schedule B-2

Column [C]: Column [A] + Column [B]

OPERATING INCOME STATEMENT - ADJUSTED TEST YEAR AND STAFF RECOMMENDED

LINE NO.	ACCT. NO.	DESCRIPTION	[A] COMPANY ADJUSTED TEST YEAR AS FILED	[B] STAFF TEST YEAR ADJUSTMENTS	REF	[C] STAFF TEST YEAR AS ADJUSTED	[D] STAFF RECOMMENDED CHANGES	[E] STAFF RECOMMENDED
1		<u>REVENUES:</u>						
2	461	Metered Water Sales	\$2,843,219	\$0		\$2,843,219	\$166,419	\$3,009,638
3	460	Water Sales - Unmetered	0	0		0	0	0
4	474	Other Operating Revenue	53,527	0		53,527	0	53,527
5		Total Operating Revenues	\$2,896,746	\$0		\$2,896,746	\$166,419	\$3,063,165
6		<u>OPERATING EXPENSES:</u>						
7	601	Salaries & Wages	\$0	\$0		\$0	\$0	\$0
8	610	Purchased Water	5,265	0		5,265	0	5,265
9	615	Purchased Power	138,933	0		138,933	0	138,933
10	618	Chemicals	14,734	0		14,734	0	14,734
11	620	Repairs & Maintenance	102,989	(6,584)	1	96,406	0	96,406
12	621	Office Supplies & Expense	0	0		0	0	0
13	630	Contract Services - Accounting	13,497	0		13,497	0	13,497
14	633	Contract Services - Legal	10,603	0		10,603	0	10,603
15	631	Contract Services - Eng	7,968	0		7,968	0	7,968
16	636	Contract Services - Other	126,034	(11,003)	1, 2	115,031	0	115,031
17	634	Management Fees	765,161	(28,894)	3	736,267	0	736,267
18	635	Contractual Services - Water Testing	5,341	8,634	1, 4	13,975	0	13,975
19	641	Rents	1,666	0		1,666	0	1,666
20	650	Transportation Expense	20,650	0		20,650	0	20,650
21	657	Insurance - General Liability	17,137	0		17,137	0	17,137
22	659	Insurance - Health & Life	0	0		0	0	0
23	666	Regulatory Commission Expense - Rate Case	50,000	(20,000)	5	30,000	0	30,000
24	675	Miscellaneous Expense	29,504	0		29,504	0	29,504
25	670	Bad Debt Expense	541	0		541	0	541
26	403	Depreciation Expense	721,109	(22,028)	7	699,081	0	699,081
27	408	Taxes Other than Income	10,350	0		10,350	0	10,350
28	408.11	Property Taxes	154,562	0	8	154,562	2,966	157,528
29	409	Income Tax	102,700	13,195	9	115,895	40,997	156,892
30		Rounding	(1)	0		(1)	0	(1)
31		Total Operating Expenses	\$2,298,743	(\$66,680)		\$2,232,063	\$43,962	\$2,276,025
32		Operating Income (Loss)	\$598,003	\$66,680		\$664,683	\$122,456	\$787,140

References:

Column [A]: Company Schedule C-1

Column [B]: Schedule TBH-11

Column [C]: Column [A] + Column [B]

Column [D]: Schedules TBH-1, TBH-2 and TBH-18

Column [E]: Column [C] + Column [D]

SUMMARY OF OPERATING INCOME STATEMENT ADJUSTMENTS - TEST YEAR

LINE NO.	ACCT. NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] Expenses Reclass ADJ No. 1 Ref. Sch TBH-12	[C] Contract Services ADJ No. 2 Ref. Sch TBH-13	[D] Mgmt. Fees ADJ No. 3 Ref. Sch TBH-14	[E] Water Testing ADJ No. 4 Ref. Sch TBH-15	[F] Rate Case ADJ No. 5 Ref. Sch TBH-16	[G] Not Used ADJ No. 6 Ref. Sch TBH-17	[H] Depr. Exp. ADJ No. 7 Ref. Sch TBH-18	[I] Prop. Tax ADJ No. 8 Ref. Sch TBH-19	[K] Income Tax ADJ No. 9 Ref. Sch TBH-20	[L] STAFF ADJUSTED
1 REVENUES:													
2	461	Metered Water Sales	\$2,843,219	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$2,843,219
3	460	Water Sales - Unmetered	0	0	0	0	0	0	0	0	0	0	0
4	474	Other Operating Revenue	53,527	0	0	0	0	0	0	0	0	0	53,527
5		Total Operating Revenues	\$2,896,746	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$2,896,746
6 OPERATING EXPENSES:													
7	601	Salaries & Wages	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
8	610	Purchased Water	5,265	0	0	0	0	0	0	0	0	0	5,265
9	615	Purchased Power	138,933	0	0	0	0	0	0	0	0	0	138,933
10	618	Chemicals	14,734	0	0	0	0	0	0	0	0	0	14,734
11	620	Repairs & Maintenance	102,989	(6,564)	0	0	0	0	0	0	0	0	96,406
12	621	Office Supplies & Expense	0	0	0	0	0	0	0	0	0	0	0
13	630	Contract Services - Accounting	13,497	0	0	0	0	0	0	0	0	0	13,497
14	633	Contract Services - Legal	10,603	0	0	0	0	0	0	0	0	0	10,603
15	631	Contract Services - Eng	7,968	0	0	0	0	0	0	0	0	0	7,968
17	636	Contract Services - Other	126,034	(1,020)	0	0	0	0	0	0	0	0	125,014
16	634	Management Fees	765,161	0	0	(28,894)	0	0	0	0	0	0	736,267
18	635	Contractual Services - Water Testing	5,341	7,604	0	0	1,030	0	0	0	0	0	13,975
19	641	Rents	1,666	0	0	0	0	0	0	0	0	0	1,666
20	650	Transportation Expense	20,650	0	0	0	0	0	0	0	0	0	20,650
21	657	Insurance - General Liability	17,137	0	0	0	0	0	0	0	0	0	17,137
22	659	Insurance - Health & Life	0	0	0	0	0	0	0	0	0	0	0
23	666	Regulatory Commission Expense - Rate Case	50,000	0	0	0	0	0	0	0	0	0	50,000
24	675	Miscellaneous Expense	29,504	0	0	0	0	0	0	0	0	0	29,504
25	670	Bad Debt Expense	541	0	0	0	0	0	0	0	0	0	541
26	403	Depreciation Expense	721,109	0	0	0	0	0	0	(22,028)	0	0	699,081
27	408	Taxes Other than Income	10,350	0	0	0	0	0	0	0	0	0	10,350
28	408.11	Property Taxes	154,562	0	0	0	0	0	0	0	0	0	154,562
29	409	Income Tax	102,700	0	0	0	0	0	0	0	0	13,195	115,895
30		Rounding	(1)	0	0	0	0	0	0	0	0	0	(1)
31		Total Operating Expenses	\$2,298,743	\$0	(\$9,983)	(\$28,894)	\$1,030	(\$20,000)	\$0	(\$22,028)	\$0	\$13,195	\$2,232,063
32		Operating Income (Loss)	\$598,003	\$0	\$9,983	\$28,894	(\$1,030)	\$20,000	\$0	\$22,028	\$0	(\$13,195)	\$664,683

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Surrebuttal Schedule TBH-12

OPERATING INCOME ADJUSTMENT NO. 1 - Expense Reclassifications			
LINE NO. DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENT	[C] STAFF RECOMMENDED
1 Repairs and Maintenance	\$102,989	(\$6,584)	\$96,406
2 Contract Services - Other	126,034	(1,020)	125,014
3 Water Testing	5,341	7,604	12,945
4 Total	\$234,364	\$0	\$234,364

References:

Column [A]: Company Schedule C-2 & Workpapers

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-13

OPERATING INCOME ADJUSTMENT NO. 2 - Contractual Services - Other Expense				
LINE		[A]	[B]	[C]
NO.	DESCRIPTION	COMPANY	STAFF	STAFF
		PROPOSED	ADJUSTMENT	RECOMMENDED
1	Contractual Services - Other Expense	\$126,034	(\$9,983)	\$116,051
2	Total	\$126,034	(\$9,983)	\$116,051

Staff Adjustments

Contractual Services - Workman's Comp (Reclass to Mgmt. Services)	\$9,983
Total Adjustment	\$9,983

References:

Column [A]: Company Schedule C-2 & Workpapers

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

OPERATING INCOME ADJUSTMENT NO. 3 - Management Fees Expense

LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENT	[C] STAFF RECOMMENDED
1	Management Fees Expense	\$765,161	(\$28,894)	\$736,267
2	Total	\$765,161	(\$28,894)	\$736,267

Staff Adjustments

Remove Management Services for Underpayment of Mar. to Nov. 2013 Ex	\$17,407
Remove Bonuses with payroll taxes for Non-Dedicated Employees	8,552
Remove Bonuses with payroll taxes for Dedicated Employees	12,918
Reclass Workman's Compensation from Contractual Services	(9,983)
Total Adjustment	\$28,894

References:

Column [A]: Company Schedule C-2 & Workpapers
Column [B]: Testimony TBH
Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-15

OPERATING INCOME ADJUSTMENT NO. 4 - Water Testing Expense				
LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENT	[C] STAFF RECOMMENDED
1	Water Testing Expense	\$5,341	\$1,030	\$6,371
2	Total	\$5,341	\$1,030	\$6,371

References:

Column [A]: Company Schedule C-2 & Workpapers

Column [B]: Testimony TBH & Staff Engineering Table M

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-16

OPERATING INCOME ADJUSTMENT NO. 5 - Rate Case Expense				
LINE		[A]	[B]	[C]
NO.	DESCRIPTION	COMPANY PROPOSED	STAFF ADJUSTMENT	STAFF RECOMMENDED
1	Rate Case Expense	\$50,000	(\$20,000)	\$30,000
2	Total	\$50,000	(\$20,000)	\$30,000

References:

Column [A]: Company Schedule C-2

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

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Surrebuttal Schedule TBH-17

OPERATING INCOME ADJUSTMENT NO. 6 - Not Used

LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENT	[C] STAFF RECOMMENDED
1	Not Used	\$0	\$0	\$0
2	Total	\$0	\$0	\$0

References:

Column [A]: Company Schedule C-2

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

OPERATING INCOME ADJUSTMENT No. 7 - Depreciation Expense							
Line	ACCT		[A]	[B]	[C]	[D]	[E]
No.	NO.	DESCRIPTION	GROSS UTILITY PLANT IN SERVICE	FULLY/NON DEPRECIABLE	DEPRECIABLE PLANT	DEPREC. RATE	EXPENSE
<i>Plant In Service</i>							
1	301	Organization Costs	\$7,541	\$7,541	\$0	0.00%	\$0
2	302	Franchise Costs	352,403	352,403	0	0.00%	0
3	303	Land & Land Rights	13,636	13,636	0	0.00%	0
4	304	Structures & Improvements	401,832		401,832	3.33%	13,381
5	307	Wells & Springs	2,142,644		2,142,644	3.33%	71,350
6	310	Power Generation Equipment	549,708		549,708	5.00%	27,485
7	311	Electric Pumping Equipment	195,407		195,407	12.50%	24,426
8	320	Water Treatment Equipment					
9	320.1	Water Treatment Plants	1,499,569		1,499,569	3.33%	49,936
10	320.2	Solutions & Feeders	46,479	46,479	0	20.00%	0
11	320.3	Point Of Use Systems	0		0	10.00%	0
12	320.4	Original Arsenic Media	417,503		417,503	6.67%	27,835
13	320.5	Regenerated Arsenic Media	150,657		150,657	40.00%	60,263
14	330	Distribution Reservoirs & Standpipes					
15	330.1	Storage Tank	1,811,998		1,811,998	2.22%	40,226
16	330.2	Pressure Tanks	36,874		36,874	5.00%	1,844
17	331	Transmission & Distribution Mains	13,281,053		13,281,053	2.00%	265,621
18	333	Services	2,256,719		2,256,719	3.33%	75,149
19	334	Meters & Meter Installations	1,489,172		1,489,172	8.33%	124,048
20	335	Hydrants	732,251		732,251	2.00%	14,645
21	336	Backflow Prevention Devices	1,660		1,660	6.67%	111
22	339	Other Plant & Misc. Equip.	0		0	6.67%	0
23	340	Office Furniture & Fixtures	160,855		160,855	6.67%	10,729
24	340.1	Computer & Software	122,607	67,883	54,724	20.00%	10,945
25	341	Transportation Equipment	139,706	123,399	16,307	20.00%	3,261
26	342	Store Equipment	0		0	4.00%	0
27	343	Tools & Work Equipment	37,840		37,840	5.00%	1,892
28	344	Laboratory Equipment	132		132	10.00%	13
29	345	Power Operated Equipment	0		0	5.00%	0
30	345	Communications Equipment	577,721		577,721	10.00%	57,772
31	347	Miscellaneous Equipment	695		695	10.00%	70
32	348	Other Intangibles	1,002,914		1,002,914	10.00%	100,291
		Rounding	-	(1)	1		0
33		Subtotal General	\$27,429,576	\$611,340	\$26,818,236		\$981,293
34		Less: Amortization of Contributions			\$7,712,717	3.66%	\$282,212
31		Staff Recommended Depreciation Expense					\$699,081
32		Company Proposed Depreciation Expense					721,109
33		Increase/(Decrease) to Depreciation Expense					(\$22,028)

OPERATING INCOME ADJUSTMENT No. 8 - Property Taxes Expense

LINE NO.	DESCRIPTION	[A]	[B]
		STAFF AS ADJUSTED	STAFF RECOMMENDED
1	Staff Adjusted Test Year Revenues	\$2,896,746	\$2,896,746
2	Weight Factor	2	2
3	Subtotal (Line 1 * Line 2)	\$5,793,492	\$5,793,492
4	Staff Recommended Revenue	2,896,746	3,063,165
5	Subtotal (Line 4 + Line 5)	\$8,690,238	\$8,856,657
6	Number of Years	3	3
7	Three Year Average (Line 5 / Line 6)	\$2,896,746	\$2,952,219
8	Department of Revenue Multiplier	2	2
9	Revenue Base Value (Line 7 * Line 8)	\$5,793,492	\$5,904,438
10	Plus: 10% of CWIP (Company Excluded)	0	0
11	Less: Net Book Value of Licensed Vehicles	11,415	11,415
12	Full Cash Value (Line 9 + Line 10 - Line 11)	\$5,782,077	\$5,893,023
13	Assessment Ratio	18.00%	18.00%
14	Assessment Value (Line 12 * Line 13)	\$1,040,774	\$1,060,744
15	Composite Property Tax Rate - Obtained from ADOR	14.85070%	14.85070%
16	Staff Test Year Adjusted Property Tax Expense (Line 14 * Line 15)	\$154,562	
17	Company Proposed Property Tax	154,562	
18	Staff Test Year Adjustment (Line 16 - Line 17)	\$0	
19	Property Tax - Staff Recommended Revenue (Line 14 * Line 15)		\$157,528
20	Staff Test Year Adjusted Property Tax Expense (Line 16)		154,562
21	Increase in Property Tax Due to Increase in Revenue Requirement		\$2,966
22	Increase in Property Tax Due to Increase in Revenue Requirement (Line 21)		\$2,966
23	Increase in Revenue Requirement		\$166,419
24	Increase in Property Tax Per Dollar Increase in Revenue (Line 22 / Line 23)		1.782084%

REFERENCES:

Line 15: Composite Tax Rate obtained from Arizona Department of Revenue

Line 17: Company Schedule C-1 Page 2

Line 21: Line 19 - Line 20

Line 23: Schedule TBH-10

SAHUARITA WATER COMPANY LLC
Docket No. W-03718A-15-0213
Test Year December 31, 2014

Surrebuttal Schedule TBH-20

OPERATING INCOME ADJUSTMENT NO. 9 - Income Tax Expense				
LINE		[A]	[B]	[C]
NO.	DESCRIPTION	COMPANY PROPOSED	STAFF ADJUSTMENT	STAFF RECOMMENDED
1	Income Tax Expense	\$102,700	\$13,195	\$115,895
2	Total	\$102,700	\$13,195	\$115,895

References:

Column [A]: Company Schedule C-2

Column [B]: Testimony TBH

Column [C]: Column [A] + Column [B]

RATE DESIGN			
Monthly Usage Charge	Present Rates	Company Proposed Rates	Staff Recommended Rates
5/8 x 3/4" Meter	\$17.15	\$19.12	\$18.35
3/4" Meter	26.80	28.68	28.00
1" Meter	42.88	47.81	43.98
1½" Meter	85.75	95.61	86.85
2" Meter	137.20	152.98	138.30
3" Meter	274.40	305.96	275.50
4" Meter	428.75	478.06	429.85
6" Meter	857.50	956.11	858.60
Commodity Rates	Present Rates	Company Proposed Rates	Staff Recommended Rates
5/8 x 3/4" & 3/4" Meter - Residential			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 3,000 Gallons	\$2.500	\$2.888	\$2.750
From 3,001 to 9,000 Gallons	3.750	4.188	3.900
Over 9,000 Gallons	4.500	4.988	4.740
5/8 x 3/4" & 3/4" Meter - Commercial & Industrial			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 9,000 Gallons	\$3.750	\$4.188	\$3.900
Over 9,000 Gallons	4.500	4.988	4.740
1" - Residential, Commercial & Industrial			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 20,000 Gallons	\$3.750	\$4.188	\$3.900
Over 20,000 Gallons	4.500	4.988	4.740
1½" - Residential, Commercial & Industrial			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 55,000 Gallons	\$3.750	\$4.188	\$3.900
Over 55,000 Gallons	4.500	4.988	4.740
2" - Residential, Commercial & Industrial			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 90,000 Gallons	\$3.750	\$4.188	\$3.900
Over 90,000 Gallons	4.500	4.988	4.740
3" - Residential, Commercial & Industrial			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 200,000 Gallons	\$3.750	\$4.188	\$3.900
Over 200,000 Gallons	4.500	4.988	4.740
4" - Residential, Commercial & Industrial			
Gallons Included in Minimum	0	0	0
Excess of Minimum - per 1,000 Gallons			
From 1 to 350,000 Gallons	\$3.750	\$4.188	\$3.900
Over 350,000 Gallons	4.500	4.988	4.740

*** Minimum \$5.00 or 1.5% per month.

SAHUARITA WATER COMPANY LLC

Surrebuttal Schedule TBH-22

Docket No. W-03718A-15-0213

Test Year December 31, 2014

TYPICAL BILL ANALYSIS

General Service 5/8 x 3/4-Inch Meter

Company Proposed	Gallons		Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	4,677		\$30.94	\$34.81	\$3.87	12.50%
Median Usage	4,500		\$30.28	\$34.07	\$3.79	12.52%
Staff Recommended						
Average Usage	4,677		\$30.94	\$33.14	\$2.20	7.12%
Median Usage	4,500		\$30.28	\$32.45	\$2.18	7.18%

Present & Proposed Rates (Without Taxes)

General Service 5/8 x 3/4-Inch Meter

Gallons	Present		Company Proposed		%	Staff Recommended		%
	Minimum Charge	\$17.15	Minimum Charge	\$19.12		Minimum Charge	\$18.35	
	1st Tier Rate	\$2.500	1st Tier Rate	\$2.888		1st Tier Rate	\$2.750	
	1st Tier Break-over	3,000	1st Tier Break-over	3,000		1st Tier Break-over	3,000	
	2nd Tier Rate	\$3.750	2nd Tier Rate	\$4.188		2nd Tier Rate	\$3.900	
	2nd Tier Break-over	9,000	2nd Tier Break-over	9,000		2nd Tier Break-over	9,000	
	3rd Tier Rate	\$4.500	3rd Tier Rate	\$4.988		3rd Tier Rate	\$4.740	

Consumption	Rates	Rates	Increase	Rates	Increase
-	\$17.15	\$19.12	11.49%	\$18.35	7.00%
1,000	\$19.65	\$22.01	12.00%	\$21.10	7.38%
2,000	\$22.15	\$24.90	12.40%	\$23.85	7.67%
3,000	\$24.65	\$27.78	12.71%	\$26.60	7.91%
4,000	\$28.40	\$31.97	12.58%	\$30.50	7.39%
5,000	\$32.15	\$36.16	12.47%	\$34.40	7.00%
6,000	\$35.90	\$40.35	12.39%	\$38.30	6.69%
7,000	\$39.65	\$44.54	12.32%	\$42.20	6.43%
8,000	\$43.40	\$48.72	12.27%	\$46.10	6.22%
9,000	\$47.15	\$52.91	12.22%	\$50.00	6.04%
10,000	\$51.65	\$57.90	12.10%	\$54.74	5.98%
11,000	\$56.15	\$62.89	12.00%	\$59.48	5.93%
12,000	\$60.65	\$67.88	11.91%	\$64.22	5.89%
13,000	\$65.15	\$72.86	11.84%	\$68.96	5.85%
14,000	\$69.65	\$77.85	11.78%	\$73.70	5.81%
15,000	\$74.15	\$82.84	11.72%	\$78.44	5.79%
16,000	\$78.65	\$87.83	11.67%	\$83.18	5.76%
17,000	\$83.15	\$92.82	11.62%	\$87.92	5.74%
18,000	\$87.65	\$97.80	11.58%	\$92.66	5.72%
19,000	\$92.15	\$102.79	11.55%	\$97.40	5.70%
20,000	\$96.65	\$107.78	11.52%	\$102.14	5.68%
25,000	\$119.15	\$132.72	11.39%	\$125.84	5.61%
30,000	\$141.65	\$157.66	11.30%	\$149.54	5.57%
35,000	\$164.15	\$182.60	11.24%	\$173.24	5.54%
40,000	\$186.65	\$207.54	11.19%	\$196.94	5.51%
45,000	\$209.15	\$232.48	11.15%	\$220.64	5.49%
50,000	\$231.65	\$257.42	11.12%	\$244.34	5.48%
75,000	\$344.15	\$382.12	11.03%	\$362.84	5.43%
100,000	\$456.65	\$506.82	10.99%	\$481.34	5.41%

Sahuarita Water Company, LLC

W-03718A-15-0213

ATTACHMENT A

**SAHUARITA WATER COMPANY, LLC
DOCKET NO. W-03718A-15-0213
RESPONSE TO STAFF'S FIRST SET OF DATA REQUESTS**

Date: August 19, 2015

Response provided by: Marian Homiak

Title: Controller

Company Name: Sahuarita Water Company, LLC

Address: 4549 East Ft Lowell Road
Tucson, AZ 85712

Company Response Number: TBH 1.34

- Q. Incentive Pay (included in the Management Fees) – Please provide the following information:
- a. A detailed explanation for any incentive plans in existence during the years of 2012, 2013 and 2014.
 - b. For all incentive plans in effect during the Test Year, please provide documentation explain how the plan works.
 - c. The total dollar amount of incentive pay included in the test year income statement of your application.
 - d. Please state the account numbers used to record incentive pay.

RESPONSE:

- a. It is the general policy for management to give, at its discretion a year-end bonus to employees for their work over the past year.
- b. There is nothing in writing and it is entirely up to the Managing Partner. Items that are considered are overall performance and vehicle use. During the year, employees are not reimbursed for the use of their private vehicles and this is also taken into consideration at the end of the year.
- c. The total dollar amount of incentive pay (bonus) included in the test year income statement of our application is:

Dedicated Employees:	\$12,000.00
Non-Dedicated Employees:	8,552.44
- d. AC#634.8

BEFORE THE ARIZONA CORPORATION COMMISSION

DOUG LITTLE
Chairman
BOB STUMP
Commissioner
BOB BURNS
Commissioner
TOM FORESE
Commissioner
ANDY TOBIN
Commissioner

IN THE MATTER OF THE APPLICATION OF)	DOCKET NO. W-03718A-15-0213
SAHUARITA WATER COMPANY, LLC AN)	
ARIZONA WATER CORPORATION, FOR A)	
DETERMINATION OF THE CURRENT FAIR)	
VALUE OF ITS UTILITY PROPERTY AND)	
FOR THE ESTABLISHMENT OF JUST AND)	
REASONABLE RATES AND CHARGES.)	
_____)	

SURREBUTTAL

TESTIMONY

OF

MICHAEL S. THOMPSON, P. E.

UTILITIES ENGINEER

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

APRIL 1, 2016

**SURREBUTTAL TESTIMONY
SAHUARITA WATER COMPANY, LLC
DOCKET NO. W-03718A-15-0213**

RECOMMENDATIONS:

1. Staff recommends that the original arsenic media be given an average useful service life of 15 years, and a depreciation rate of 6.67 percent.
2. Staff further recommends that regenerated arsenic media be given an average useful service life of 2 ½ years, and a depreciation rate of 40 percent.
3. Staff further recommends that SWC use the Staff recommended depreciation rates shown in Exhibit MST-1.

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EXHIBIT

DEPRECIATION RATE TABLE.....	MST-1
------------------------------	-------

1 **INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. My name is Michael Thompson. My business address is 1200 West Washington Street,
4 Phoenix, Arizona 85007.

5
6 **Q. By whom and in what position are you employed?**

7 A. I am employed by the Arizona Corporation Commission ("Commission" or "ACC") as a
8 Utilities Engineer - Water/Wastewater in the Utilities Division.

9
10 **Q. Did you submit Direct Testimony on behalf of the ACC Utilities Division Staff**
11 **("Staff") in this case?**

12 A. Yes.

13
14 **PURPOSE OF TESTIMONY**

15 **Q. What is the purpose of your Surrebuttal Testimony?**

16 A. To respond to the Rebuttal Testimony filed by Geoff Caron on behalf of Sahuarita Water
17 Company, LLC ("SWC"). My testimony addresses Mr. Caron's comments regarding the
18 depreciation of the original and regenerated arsenic media.

19
20 **ORIGINAL & REGENERATED ARSENIC MEDIA DEPRECIATION**

21 **Q. Does Staff agree with Mr. Caron's recommended depreciation rates for the original**
22 **and regenerated arsenic media?**

23 A. Yes. After an extensive conversation with Mr. Caron and a review of additional information
24 provided by SWC, Staff was able to reach a better understanding of the
25 operational/performance aspects of the arsenic media. Therefore, Staff has modified its
26 position and is recommending that the original arsenic media be given an average useful

1 service life of 15 years, and a depreciation rate of 6.67 percent. Staff further recommends
2 that regenerated arsenic media be given an average useful service life of 2 ½ years, and a
3 depreciation rate of 40 percent.
4

5 **Q. Has Staff revised its depreciation rate table to reflect the National Association of**
6 **Regulatory Utility Commissioners (“NARUC”) Accounts for the original and**
7 **regenerated arsenic media?**

8 A. Yes. Staff revised the depreciation table to include NARUC Account No. 320.4 – Arsenic
9 Media, and NARUC Account No. 320.5 – Regenerated Arsenic Media. Staff’s revised
10 depreciation table, attached to this testimony, is shown on Exhibit MST-1. Staff
11 recommends that SWC use the Staff recommended depreciation rates shown in Exhibit
12 MST-1.
13

14 **Q. Does this conclude your Surrebuttal Testimony?**

15 A. Yes, it does.

DEPRECIATION RATES FOR WATER COMPANIES

NARUC Account No.	Depreciable Plant	Average Service Life (Years)	Annual Accrual Rate (%)
301	Organization	----	0.00
302	Franchises	----	0.00
303	Land and Land Rights	----	0.00
304	Structures & Improvements	30	3.33
305	Collecting & Impounding Reservoirs	40	2.50
306	Lake, River, Canal Intakes	40	2.50
307	Wells & Springs	30	3.33
308	Infiltration Galleries	15	6.67
309	Raw Water Supply Mains	50	2.00
310	Power Generation Equipment	20	5.00
311	Pumping Equipment	8	12.5
320	Water Treatment Equipment		
320.1	Water Treatment Plants	30	3.33
320.2	Solution Chemical Feeders	5	20.00
320.3	Point-of-Use Treatment Devices	10	10.00
320.4	Arsenic Treatment Media	15	6.67
320.5	Arsenic Treatment Media Regeneration	2.5	40.00
330	Distribution Reservoirs & Standpipes		
330.1	Storage Tanks	45	2.22
330.2	Pressure Tanks	20	5.00
331	Transmission & Distribution Mains	50	2.00
333	Services	30	3.33
334	Meters	12	8.33
335	Hydrants	50	2.00
336	Backflow Prevention Devices	15	6.67
339	Other Plant & Misc. Equipment	15	6.67
340	Office Furniture & Equipment	15	6.67
340.1	Computers & Software	5	20.00
341	Transportation Equipment	5	20.00
342	Stores Equipment	25	4.00
343	Tools, Shop & Garage Equipment	20	5.00
344	Laboratory Equipment	10	10.00
345	Power Operated Equipment	20	5.00
346	Communication Equipment	10	10.00
347	Miscellaneous Equipment	10	10.00
348	Other Tangible Plant	10	10.00

BEFORE THE ARIZONA CORPORATION COMMISSION

DOUG LITTLE
Chairman
BOB STUMP
Commissioner
BOB BURNS
Commissioner
TOM FORESE
Commissioner
ANDY TOBIN
Commissioner

IN THE MATTER OF THE APPLICATION OF)	DOCKET NO. W-03718A-15-0213
SAHUARITA WATER COMPANY, LLC, FOR A)	
DETERMINATION OF THE CURRENT FAIR)	
VALUE OF ITS UTILITY PROPERTY AND FOR)	
THE ESTABLISHMENT OF JUST AND)	
REASONABLE RATES AND CHARGES)	
<hr/>		

SURREBUTTAL

TESTIMONY

OF

CRYSTAL S. BROWN

EXECUTIVE CONSULTANT III

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

APRIL 1, 2016

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EXECUTIVE SUMMARY
SAHUARITA WATER COMPANY, LLC,
DOCKET NO. W-03718A-15-0213

Staff continues to recommend an 8.41 percent rate of return. Staff's recommended rate of return was calculated using a 9.50 percent cost of equity, a 4.20 percent cost of debt, and a capital structure consisting of 20.57 percent debt and 79.43 percent equity.

I. INTRODUCTION

Q. Please state your name, occupation, and business address.

A. My name is Crystal S. Brown. I am an Executive Consultant III employed by the Arizona Corporation Commission ("Commission") in the Utilities Division ("Staff"). My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

Q. Are you the same Crystal S. Brown who filed direct testimony in this case?

A. Yes, I am.

Q. What is the purpose of your surrebuttal testimony in this rate proceeding?

A. The purpose of my surrebuttal testimony is to respond to the cost of capital rebuttal testimony of Sahuarita Water Company's ("Sahuarita" or "Company") witness, Thomas J. Bourassa.

Q. Please explain how Staff's surrebuttal testimony is organized.

A. Staff's surrebuttal testimony is presented in three sections. Section I is this introduction. Section II presents Staff's comments on the rebuttal testimony of the Company's cost of capital witness, Mr. Bourassa. Lastly, Section III presents Staff's recommendations.

II. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY FILED BY THE COMPANY'S COST OF CAPITAL WITNESS, MR. THOMAS J. BOURASSA

Q. Please summarize the capital structure, cost of debt, cost of equity, and overall weighted average cost of capital proposed in Mr. Bourassa's rebuttal testimony.

A. In his rebuttal testimony, Mr. Bourassa is proposing a capital structure consisting of 20.57 percent debt and 79.43 percent equity. Mr. Bourassa proposes a 10.5 percent cost of equity

1 (“COE”) and a 4.2 percent cost of debt for the Company. Mr. Bourassa’s cost of capital
2 proposals result in an overall rate of return (“ROR”) for Sahuarita of 9.2 percent.

3
4 The 10.5 percent rebuttal return on equity (“ROE”) proposal being made by Mr. Bourassa is
5 the same as his 10.5 percent ROE proposal found in his direct testimony. Staff’s ROE
6 recommendation is 9.5 percent in both its direct and surrebuttal cost of capital filings.

7
8 **Q. Is there a primary conceptual basis for the difference in the ROE proposals of the**
9 **Company and the ROE recommendations supported by Staff?**

10 A. Yes. The Company follows what is called a company-specific approach to developing its
11 ROE proposal, whereas Staff follows the portfolio approach to defining its fair and
12 reasonable ROE recommendation. I will discuss the differences in these two approaches in
13 my testimony but generally both approaches rely on the results generated from application of
14 the discounted cash flow (“DCF”) and capital asset pricing model (“CAPM”) ROE models.
15 The Company then adds the results of a number of company-specific risk considerations
16 whereas, under Staff’s portfolio approach, such risk adders are *not directly* given consideration
17 because in the capital markets such risks can be, *and are*, addressed by diversification of the
18 investor’s portfolio so ratepayers *should not* be required to compensate for a risk that can be
19 reasonably, and simply, addressed through an investment tool existing in the market place.
20 That tool is “portfolio diversification.”

21
22 On page 5, line 21, of Mr. Bourassa’s rebuttal testimony he says that investors “do not
23 ignore” the various company-specific risks that exist. Staff agrees with this statement which
24 is exactly why prudent investors diversify their portfolios. And since portfolio diversification
25 is both a simple and logical step for investors to take to safeguard their investments from

1 such risks, there is no reason for ratepayers to be required to compensate investors for these
2 risks.

3
4 *Comments Regarding Staff's Range of COEs*

5 **Q. Did Staff review the Company's comments concerning Staff's position that any COE**
6 **in Staff's range of COE's is reasonable?**

7 A. Yes.

8
9 **Q. What were the Company's comments?**

10 A. Mr. Bourassa concludes on page 14, line 7, that "... the mid-point (and sometimes the
11 median) is arguably the most 'fair' estimate ..." of a range of COE's, but he goes on to
12 suggest that under the *Bluefield* and *Hope* standards further specific consideration of other risk
13 factors must be made, which then leads Mr. Bourassa into a lengthy discussion of other
14 company-specific risk considerations that he ultimately suggests he has been able to
15 specifically measure from the perspective of Sahuarita Water, e.g., risk "X" requires a "19"
16 basis point adjustment whereas risk "Z" requires a further "17" basis point adjustment to
17 ROEs.

18
19 **Q. Does Staff agree?**

20 A. No, Staff does not. The *Hope* and *Bluefield* Supreme Court decisions which Mr. Bourassa
21 makes reference to set forth the standard criteria which must result from a Commission's
22 ROE decision in order to conclude that the ROE constitutes a fair rate of return. Staff notes
23 that those court decisions do not:

- 24
25 1. Prescribe the *types of COE models* to be used
26 2. Prescribe that a certain *number of COE models* be used, and

1 3. Prescribe that an *exact point within a range of COE's* be used

2
3 Rather, the *Hope* and *Bluefield* Supreme Court decisions identify certain criteria that must be
4 met for a rate of return to be deemed "fair." Those criteria are capital attraction, financial
5 integrity, and comparable earnings. The DCF and CAPM models are foundational cost of
6 capital ("COC") models that have been recognized as models that generate results that meet
7 these criteria. Also, these models are widely used by other public utility commissions; are
8 taught in National Association of Regulatory Utility Commissioners ("NARUC") training
9 classes; and have been adopted for establishing reasonable ROE ranges by this Commission
10 for at least 25 years.

11
12 Therefore, since the DCF and CAPM models produce results that meet the fairness standards
13 of the *Hope* and *Bluefield* court cases and Staff used the DCF and CAPM models to calculate
14 each of the points in Staff's ROE reasonableness range, then any point in Staff's range of
15 COE's is reasonable and fair.

16
17 *Comments Regarding Moving Higher Than the Low Point of Staff's Model-Driven ROE Range*

18 **Q. Would you please clarify Staff's statement that "moving higher than the low point of**
19 **the range makes a reasonable acknowledgement of, or concession to, the other risk**
20 **factors"?**

21 A. Yes. First, let me say that Staff acknowledges that all models or approaches used to defining
22 a fair ROE range can have shortcomings, even if what are termed to be shortcomings are
23 simply differences of professional judgement regarding the assumptions to be made in
24 generating results from these generally accepted models. There is no perfect or absolute way
25 to determine "required return" in a constantly changing financial marketplace. So, by moving
26 above the low result from Staff's model-driven ROE range, Staff is merely trying to find

1 common ground with those who are of the opinion that investors actually require a higher
2 ROE because of consideration "A" or "B".

3
4 **Q. By suggesting that any point within its model-driven ROE range would be a**
5 **reasonable ROE for the Commission to authorize, and by using an ROE above the**
6 **low point of Staff's model-driven ROE range in its revenue requirement schedules, is**
7 **Staff also attempting to find common ground with parties that might argue that one**
8 **more model variation, or one more approach to developing the ROE range should be**
9 **given consideration?**

10 A. Yes.

11
12 *Compensation for Company Specific Risk*

13 **Q. Should investors expect to be compensated for company-specific risk?**

14 A. No, they should not. The type of risk that investors should expect to be compensated for are
15 systematic risks (i.e., market risks). Quite simply, market risks cannot be diversified away
16 because investors can and certainly do diversify their investment portfolios as the means for
17 effectively safeguarding their investments from company-specific risk. This point is made on
18 page 52 of Mr. Roger Morin, Ph.D.'s book *Regulatory Finance, Utilities' Cost of Capital*, where he
19 states, "Thus, for a diversified investor, the relevant risk of a security is reduced to its market
20 risk, or beta, the risk that cannot be diversified away." Therefore, investors should not be
21 expected to be compensated for company-specific risks as those risks can be diversified away.

22
23 In Staff's opinion, anyone who argues that investors must be directly compensated for
24 company-specific risk is also arguing that for some reason ratepayers must step up and
25 compensate for a specific investor's failure to take advantage of a simple investment tool –
26 that being portfolio diversification. Such advocates typically go to great lengths to suggest

1 that they have developed a way to quantify exactly what level of compensation an investor
2 requires for each element of company-specific risk. This is totally unnecessary. The failure
3 on the part of an investor to diversify his/her portfolio is *not* a decision that should become a
4 financial obligation of ratepayers.

5
6 **Q. Is systematic (i.e., market) risk addressed and incorporated in both the DCF model**
7 **and the CAPM?**

8 A. Yes. The DCF Model is a cash flow assessment tool used to derive the COE. For the DCF,
9 it is assumed that all cash flow items have equivalent exposure to systematic risk. For the
10 CAPM, systematic risk is reflected in the Beta which measures a stock's riskiness compared to
11 the market as a whole.

12
13 *Comments Regarding Comparing Staff's Recommended COE to that of the Proxy Group*

14 **Q. Mr. Bourassa asserted that investors would be better off investing in publically traded**
15 **companies (i.e., his proxy group of companies) than from investing in Sahuarita**
16 **Water. This discussion starts on page 8 of Mr. Bourassa's rebuttal testimony and the**
17 **actual statement regarding such assertion appears on page 10 of this testimony. Is**
18 **this a reasonable comparison?**

19 A. No, it is not. An investor in the proxy group does not have the same level of influence over
20 management decisions as do principal investors in Sahuarita. The influence of the principal
21 investors includes, but is not limited to, controlling the amount and timing of rate increases,
22 plant additions, and having complete access to the cash provided by operating income and
23 depreciation expense. The principal investors can use this cash for any purpose they choose.

24
25 Staff does not intend to get into a lengthy discussion regarding this point, but this ability to
26 influence management decision making to the benefit of the primary investors in Sahuarita is

1 an observable reality, and the value of such influence is omitted by Mr. Bourassa as he
2 discusses and then quantifies the firm-specific risks faced by Sahuarita's investors.

3
4 For example, Schedule E-2 of the Company's application shows that Sahuarita reported
5 operating income during the years 2012 to 2014 of \$974,050 in 2012, \$764,382 in 2013, and
6 \$739,570 in 2014. As shown on Schedule E-4, the amount of distributions during the same
7 period were \$328,049 in 2012, \$450,000 in 2013, and \$2,067,562 in 2014. Effectively,
8 Sahuarita's principal investors were able to "draw" \$367,609¹ more than the Company made
9 during this period of time. This suggests a significant ability to influence management's
10 distribution making decisions that investors in the proxy group do not have.

11
12 This ability to influence management decisions is one of the main reasons why Sahuarita's
13 ROE should not be unequivocally compared to the achieved and forecasted ROE's of the
14 proxy group as Mr. Bourassa has done. Instead, a reasonable comparison would be to the
15 ROEs recently authorized by the Commission for other ACC-regulated water and wastewater
16 companies.

17
18 **III. STAFF RECOMMENDATIONS**

19 **Q. In updating its COC analysis for the Company, did Staff's recommended ROE and**
20 **overall ROR change from the levels recommended by Staff in direct testimony?**

21 A. No, it did not. Staff recommended the highest COE in the range; this COE did not change
22 after the update was performed.

23
24 **Q. What are Staff's recommendations for the Company?**

25 A. Staff recommends the following for Sahuarita's cost of capital:

¹ (\$974,050 + \$764,382 + \$739,570) - (\$328,049 + \$450,000 + \$2,067,562) = -\$367,609

- 1 1. A capital structure of 20.57 percent debt and 79.43 percent equity.
- 2 2. A 4.20 percent cost of debt.
- 3 3. A 9.50 percent return on equity.
- 4 4. An 8.41 percent overall rate of return.

5

6 **Q. Does this conclude your surrebuttal testimony?**

7 A. Yes, it does.

Sahuarita Water Company, Inc. Cost of Capital Calculation
Capital Structure
And Weighted Average Cost of Capital
Staff Recommended and Company Proposed

[A]	[B]	[C]	[D]
Description	Weight (%)	Cost	Weighted Cost
Staff Recommended Capital Structure			
Debt	20.57%	4.20%	0.86%
Common Equity	79.43%	9.50%	7.55%
Weighted Average Cost of Capital			8.41%
Company Proposed Capital Structure			
Debt	20.57%	4.20%	0.86%
Common Equity	79.43%	10.50%	8.34%
Weighted Average Cost of Capital			9.20%

[D] : [B] x [C]

Supporting Schedules: CSB-3 and CSB-4.

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Sahuarita Water Company, Inc. Cost of Capital Calculation

Final Cost of Equity Estimates

Sample Water Utilities

[A]	[B]	[C]	[D]	[E]
<u>DCF Method</u>				
Constant Growth DCF Estimate		D_1/P_a ¹	+	g ² = <u>k</u>
Multi-Stage DCF Estimate		2.3%	+	5.6% = 7.9%
Average DCF Estimate				<u>8.7%</u> 8.30%
<u>CAPM Method</u>				
Historical Market Risk Premium ³	R_f	β ³	x	(R_p) = <u>k</u>
Current Market Risk Premium ⁴	2.1%	0.73	x	7.6% ⁶ = 7.6%
Average CAPM Estimate	2.9%	0.73	x	9.2% ⁷ = <u>9.5%</u> 8.60%
Staff's Estimated Cost of Equity				
Economic Assessment Adjustment				
Sub-Total				
Financial Risk Adjustment				
Total				
				<u>9.5%</u> 9.50% <u>9.50%</u> 9.50%

1 MSN Money and Value Line

2 Schedule JAC-8

3 Risk-free rate (Rf) for 5, 7, and 10 year Treasury rates from the U.S. Treasury Department at www.ustreas.gov4 Risk-free rate (Rf) for 30 Year Treasury bond rate from the U.S. Treasury Department at www.ustreas.gov

5 Value Line

6 Historical Market Risk Premium (Rp) calculated from 2015 Ibbotson SBBI Classic Yearbook data

7 Testimony

Sahuarita Water Company, Inc. Cost of Capital Calculation
Average Capital Structure of Sample Water Utilities

[A]	[B]	[C]	[D]
<u>Company</u>	<u>Debt</u>	<u>Common Equity</u>	<u>Total</u>
American States Water	38.7%	61.3%	100.0%
California Water	45.9%	54.1%	100.0%
Aqua America	50.3%	49.7%	100.0%
Connecticut Water	45.6%	54.4%	100.0%
Middlesex Water	44.3%	55.7%	100.0%
SJW Corp	54.7%	45.3%	100.0%
York Water	<u>43.4%</u>	<u>56.6%</u>	<u>100.0%</u>
 Average Sample Water Utilities	 46.1%	 53.9%	 100.0%
 Sahuarita	 20.57%	 79.43%	 100.0%

Source:

Sample Water Companies from Value Line

Sahuarita Water Company, Inc. Cost of Capital Calculation
Growth in Earnings and Dividends
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]
	Dividends Per Share 2005 to 2014	Dividends Per Share Projected	Earnings Per Share 2005 to 2014	Earnings Per Share Projected
<u>Company</u>	<u>DPS¹</u>	<u>DPS¹</u>	<u>EPS¹</u>	<u>EPS¹</u>
American States Water	6.4%	6.7%	11.6%	6.5%
California Water	1.4%	8.3%	5.0%	5.4%
Aqua America	7.8%	9.7%	8.9%	6.6%
Connecticut Water	1.9%	5.2%	5.2%	3.2%
Middlesex Water	1.4%	2.3%	4.5%	3.6%
SJW Corp	3.9%	1.3%	8.5%	NA
York Water	<u>3.9%</u>	<u>6.7%</u>	<u>6.1%</u>	<u>5.3%</u>
Average Sample Water Utilities	3.8%	5.7%	7.1%	5.1%

1 Value Line

Sahuarita Water Company, Inc. Cost of Capital Calculation
Sustainable Growth
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]
<u>Company</u>	Retention Growth 2005 to 2014 <u>br</u>	Retention Growth Projected <u>br</u>	Stock Financing Growth <u>vs</u>	Sustainable Growth 2005 to 2014 <u>br + vs</u>	Sustainable Growth Projected <u>br + vs</u>
American States Water	4.6%	7.0%	1.6%	6.2%	8.5%
California Water	2.9%	3.6%	1.4%	4.3%	5.0%
Aqua America	4.3%	5.7%	1.2%	5.5%	6.9%
Connecticut Water	2.3%	4.1%	3.4%	5.7%	7.5%
Middlesex Water	1.6%	3.6%	2.0%	3.6%	5.6%
SJW Corp	4.0%	4.2%	1.1%	5.0%	5.2%
York Water	<u>2.4%</u>	<u>3.8%</u>	<u>3.0%</u>	<u>5.4%</u>	<u>6.8%</u>
Average Sample Water Utilities	3.1%	4.6%	2.0%	5.1%	6.5%

[B]: Value Line

[C]: Value Line

[D]: Value Line, Yahoo Finance, and Form 10-Ks filed with the Securities and Exchange Commission (<http://www.sec.gov/>)

[E]: [B]+[D]

[F]: [C]+[D]

Sahuarita Water Company, Inc. Cost of Capital Calculation
Selected Financial Data of Sample Water Utilities

[A] [B] [C] [D] [E] [F] [G]

<u>Company</u>	<u>Symbol</u>	<u>Spot Price</u> <u>3/17/2016</u>	<u>Book Value</u>	<u>Mkt To</u> <u>Book</u>	<i>Value Line</i>	Raw
					Beta	Beta
American States Water	AWR	38.72	13.97	2.8	0.70	0.52
California Water	CWT	26.18	13.48	1.9	0.75	0.60
Aqua America	WTR	32.13	9.57	3.4	0.75	0.60
Connecticut Water	CTWS	43.76	21.34	2.1	0.65	0.45
Middlesex Water	MSEX	30.74	12.61	2.4	0.75	0.60
SJW Corp	SJW	36.28	17.26	2.1	0.75	0.60
York Water	YORW	30.49	8.71	<u>3.5</u>	<u>0.75</u>	<u>0.60</u>
Average				2.6	0.73	0.57

[C]: Msn Money

[D]: Value Line

[E]: [C] / [D]

[F]: Value Line

[G]: $(-0.35 + [F]) / 0.67$

Sahuarita Water Company, Inc. Cost of Capital Calculation
Calculation of Expected Infinite Annual Growth in Dividends
Sample Water Utilities

[A]	[B]
<u>Description</u>	<u>g</u>
DPS Growth - Historical ¹	3.8%
DPS Growth - Projected ¹	5.7%
EPS Growth - Historical ¹	7.1%
EPS Growth - Projected ¹	5.1%
Sustainable Growth - Historical ²	5.1%
<u>Sustainable Growth - Projected²</u>	<u>6.5%</u>
Average	5.6%

1 Schedule CSB-5

2 Schedule CSB-6

Sahuarita Water Company, Inc. Cost of Capital Calculation
Multi-Stage DCF Estimates
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]	[G]	[H]
<u>Company</u>	Current Mkt. Price (P_0) ¹ 3/17/2016	Projected Dividends ² (Stage 1 growth) (D_t)				Stage 2 growth ³ (g_n)	Equity Cost Estimate (K) ⁴
		d_1	d_2	d_3	d_4		
American States Water	38.7	0.90	0.95	1.00	1.06	6.4%	8.7%
California Water	26.2	0.67	0.71	0.75	0.79	6.4%	8.9%
Aqua America	32.1	0.70	0.74	0.78	0.82	6.4%	8.5%
Connecticut Water	43.8	1.08	1.14	1.21	1.27	6.4%	8.8%
Middlesex Water	30.7	0.77	0.81	0.86	0.91	6.4%	8.9%
SJW Corp	36.3	0.78	0.83	0.87	0.92	6.4%	8.5%
York Water	30.5	0.60	0.63	0.67	0.71	6.4%	8.3%

$$P_0 = \sum_{t=1}^n \frac{D_t}{(1+K)^t} + \frac{D_n(1+g_n)}{K-g_n} \left[\frac{1}{(1+K)} \right]^n$$

Average 8.7%

Where : P_0 = current stock price
 D_t = dividends expected during stage 1
 K = cost of equity
 n = years of non – constant growth
 D_n = dividend expected in year n
 g_n = constant rate of growth expected after year n

1 [B] see Schedule CSB-7

2 Derived from Value Line Information

3 Average annual growth in GDP 1929 - 2012 in current dollars.

4 Internal Rate of Return of Projected Dividends

Sahuarita Water Company, Inc. Cost of Capital Calculation Capitalization				
	<u>Interest Rate</u>	<u>Annual Interest</u>	<u>Amount outstanding as of 12/31/2014</u>	<u>Percentage of Capital Structure</u>
Long-Term Debt				
WIFA Loan	4.20%	\$ 97,693	\$ 2,326,035	
Long-Term Debt		\$ 97,693	\$ 2,326,035	20.57%
Short-Term Debt		\$ -		0.00%
Total Debt	4.20%	\$ 97,693	\$ 2,326,035	20.57%
Common Equity			\$ 8,982,660	
Common Shares Outstanding				
Paid in Capital				
Retained Earnings				
Total Common Equity			\$ 8,982,660	79.43%
Total Capitalization			\$ 11,308,695	100.00%